

Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred incident to sales of service. See 86 Ill. Adm. Code Part 140. (This is a GIL).

April 1, 2002

Dear Xxxxx:

This letter is in response to your letter received January 16, 2002. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120(b) and (c), which can be found on the Department's website at www.revenue.state.il.us/Laws/regs/part1200/.

In your letter, you have stated and made inquiry as follows:

The purpose of this letter is to request a written opinion from the Department of Revenue concerning the correct handling of Illinois sales and use taxes in the following situation.

SITUATION

I have a client, who we can call 'Company A', located in STATE and they plan to expand their business activities into your state. Company A has several services that they offer. The work will be done initially using vendors in your state that Company A has contacted and it is anticipated that Company A will have some of its own employees working in your state in the next twelve months. The services that Company A will offer are as follows:

- A. Company A installs DSL on computers for clients of large Internet service providers. The way this works is as follows: A customer calls up one of the large Internet service providers and signs up to get connected to the internet using DSL. The Internet service provider calls up Company A and asks them to go to their client and install the DSL on their customer's computer. Company A goes out to the customer and installs the DSL on the customer's computer. The Internet service provider provides all of the materials to Company A. Company A only provides the installation service, not the materials. Company A bills the Internet service provider for the DSL installation. The Internet service provider bills their customer for DSL installation and any materials.
- B. Company A installs and services Local Area Networks 'LAN'. Local Area Networks are used to connect workstations and personal computers. The LAN allows users to communicate with each other, share data and share printers. The

installation involves running cable between the computers and connecting the cables to a hub, so that the signals can be routed to the correct device. Company A will install, service and sell the materials needed to install and service the LAN. This work will be performed and billed to the end user. The work will be billed on a time and material basis.

- C. Company A will provide ongoing support to customers with Local Area Networks. This service will be to troubleshoot, reconfigure and upgrade the LAN. This support will be billed on an annual, monthly or per incident basis. This support will be primarily service, however there may be some small charges for materials.
- D. Company A will maintain a 'Help Desk' at their location in STATE. The Help Desk will take phone calls from customers located throughout the United States. The nature of the calls will be customers looking for assistance troubleshooting problems with their Local Area Networks. The customers will be provided assistance for free during the first fifteen minutes and a charge per minute after the first fifteen minutes.

QUESTIONS

1. If Company A's only connection with your state is through vendors that have been hired to provide the service in your state, will that create nexus and require Company A to collect sales tax on their taxable sales?
2. Is the installation of the DSL, as described in example A above, subject to sales tax in your state? If the installation is taxable, can Company A accept a resale certificate from the Internet service provider who is rebilling the charge back to their customer?
3. Are the separate charges for labor and materials during the installation of a Local Area Network, as described in example B above, subject to sales tax? If Company A provides service for a Local Area Network where they did not sell the equipment to the customer, is the labor charge for the service call taxable?
4. Will the charges for ongoing support, as described in example C above be subject to sales tax? Would the answer be different if Company A did not sell the equipment to the customer they were working on? If the labor and the materials are separated on the billing, are they both subject to sales tax?
5. Will the charges for providing troubleshooting over the phone, as described in example D above be subject to sales tax?
6. Assuming some of the services above are taxable, can the materials, which are sold to the customer, be purchased tax-free?
7. Assuming some of the services above are taxable, what rate of tax does Company A collect on the taxable sales?
8. What other taxes (i.e. state income, franchise or employment) would Company A be subject to based on the facts as described above?

Would you please provide any publications and forms that will help my client become more knowledgeable with your state's tax laws and rules and assist them in complying with your state laws? If you have any questions or need any additional information regarding the above situation, please call me. Your assistance in this matter is greatly appreciated.

Retailers' Occupation Tax and Use Tax do not apply to receipts from sales of personal services. Under the Service Occupation Tax Act, servicemen are taxed on tangible personal property transferred incident to sales of service. For your general information we are enclosing a copy of 86 Ill. Adm. Code Part 140 regarding sales of service and Service Occupation Tax. If no tangible personal property is transferred incident to a sale of service by the serviceman, no Service Occupation Tax liability is incurred. This appears to be the case with your DSL installation.

The purchase of tangible personal property that is transferred to service customers may result in either Service Occupation Tax liability or Use Tax liability for the servicemen, depending upon which tax base the servicemen choose to calculate their liability. Servicemen may calculate their tax base in one of four ways: (1) separately stated selling price; (2) 50% of the entire bill; (3) Service Occupation Tax on cost price if they are registered de minimis servicemen; or, (4) Use Tax on cost price if the servicemen are de minimis and are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act.

Using the first method, servicemen may separately state the selling price of each item transferred as a result of sales of service. The tax is based on the separately stated selling price of the tangible personal property transferred. If servicemen do not wish to separately state the selling price of the tangible personal property transferred, those servicemen must use the second method where they will use 50% of the entire bill to their service customers as the tax base. Both of the above methods provide that in no event may the tax base be less than the cost price of the tangible personal property transferred. Under these methods, servicemen may provide their suppliers with Certificates of Resale when purchasing the tangible personal property to be transferred as a part of the sales of service. Upon selling their product, they are required to collect the corresponding Service Use Tax from their customers. See 86 Ill. Adm. Code 140.106.

The third way servicemen may account for their tax liability only applies to de minimis servicemen who have either chosen to be registered or are required to be registered because they incur Retailers' Occupation Tax liability with respect to a portion of their business. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in graphic arts production). See, 86 Ill. Adm. Code 140.101(f) enclosed. This class of registered de minimis servicemen is authorized to pay Service Occupation Tax (which includes local taxes) based upon the cost price of tangible personal property transferred incident to sales of service. Servicemen that incur Service Occupation Tax collect the Service Use Tax from their customers. They remit the tax to the Department by filing returns and do not pay tax to suppliers. They provide suppliers with Certificates of Resale for the property transferred to service customers. See 86 Ill. Adm. Code 140.108.

The final method of determining tax liability may be used by de minimis servicemen that are not otherwise required to be registered under Section 2a of the Retailers' Occupation Tax Act. Servicemen may qualify as de minimis if they determine that their annual aggregate cost price of tangible personal property transferred incident to sales of service is less than 35% of their annual gross receipts from service transactions (75% in the case of pharmacists and persons engaged in

graphic arts production). Such de minimis servicemen may pay Use Tax to their suppliers or may self-assess and remit Use Tax to the Department when making purchases from unregistered out-of-State suppliers. Those servicemen are not authorized to collect "tax" from their service customers because they, not their customers, incur the tax liability. Those servicemen are also not liable for Service Occupation Tax. It should be noted that servicemen no longer have the option of determining whether they are de minimis using a transaction by transaction basis. See 86 Ill. Adm. Code 140.109.

I hope this information is helpful. The Department of Revenue maintains a website, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Melanie A. Jarvis
Associate Counsel

MAJ:msk
Enc.